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OMB Releases the 2020 Compliance Supplement Addendum

As promised, the Office of Management and Budget (OMB) has released an Addendum to the 2020 OMB Compliance Supplement that addresses new COVID-19-related programs, provides information on modified compliance requirements that are relevant to COVID-19 funding for existing programs, adds one new non-COVID-19-related cluster, includes other requirements and guidance, and extends certain single audit reporting package deadlines. The Addendum is effective for audits of fiscal years beginning after June 30, 2019, and must be used in conjunction with the 2020 Compliance Supplement to determine appropriate audit procedures.

The Addendum makes a number of modifications to the 2020 Compliance Supplement, including the following:

- Adds an addendum-specific table of contents
- Adds a supplementary Part 2 matrix
- Adds new cross-cutting provisions in Part 3 in the Reporting section for subrecipient reporting requirements under the Federal Funding Accountability and Transparency Act (FFATA)
- Adds additional programs to Part 4 with new compliance requirements as a result of COVID-19 funding, as well as one new cluster unrelated to COVID-19
- Updates Part 5 for COVID-19 considerations for the Student Financial Assistance cluster
- Updates Part 8, Appendix VII related to audit due dates, donated personal protective equipment, and other matters

The key provisions of the Addendum are summarized in this article. However, auditors and recipients of COVID-19-related funding need to review the Addendum in its entirety in order to ensure its guidance is appropriately applied to their single audits.

In this Issue:

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Practical Consideration:

The Compliance Supplement Addendum can be accessed at **www.whitehouse.gov/omb/management/office-federal-financial-management/** (single PDF file) or at **www.aicpa.org/interestareas/governmentalauditquality/resources/singleaudit/2020-omb-compliance-supplement.html** (separate PDF files by section as split out by the AICPA's Governmental Audit Quality Center).

Federal Funding Accountability and Transparency Act (FFATA) Reporting

For audits of fiscal years ending on or before September 30, 2020, auditors must test FFATA reporting for all COVID-19-related programs included in the Addendum, with the exception of the Coronavirus Relief Fund (CFDA/Assistance Listing No. 21.019), *if*:

- The reporting compliance requirement is marked as "Y" in the Part 2 matrix and the auditor determines reporting to be direct and material; and
- The direct recipient makes first-tier subawards of $25,000 or more and is therefore required to report subaward data through the FFATA Subaward Reporting System.

For audits of fiscal years ending after September 30, 2020, auditors will need to test this requirement for *all* major programs, regardless of whether the funding is COVID-19-related. In addition, the Addendum requires auditors to report specific information for noncompliance findings related to FFATA reporting. To assist the auditor in providing the required information, the Addendum includes a recommended table format for these findings that can be used in the Schedule of Findings and Questioned Costs.

Practical Consideration:

FFATA's reporting requirements relate to subaward reporting by primary recipients for virtually all federal grants and cooperative agreements. All agencies are to collect (and recipients and subrecipients are to report) specific data related to subaward reporting. Part 3, Section L, of the 2020 Compliance Supplement Addendum provides an in-depth discussion of FFATA's reporting requirements as well as suggested audit procedures.

New and Existing COVID-19 Programs Included in the Addendum

The Addendum adds a supplementary Part 2 matrix that contains a number of new COVID-19-related programs, existing programs that received additional COVID-19-related funding, and one new non-COVID-19 cluster. In addition to the matrix, Part 4 has been expanded to outline the compliance requirements for these programs in more detail. In addition to Student Financial Assistance programs, the Addendum addresses the following federal programs:

- New COVID-19-related programs:
  - 16.034 Coronavirus Emergency Supplemental Funding
  - 21.019 Coronavirus Relief Fund
  - 32.006 COVID-19 Telehealth Program
  - 84.425 Education Stabilization Fund
  - 93.461 COVID-19 Testing for the Uninsured
  - 93.498 Provider Relief Fund
- Existing programs with COVID-19-related funding:
  - 10.001 Multiple Program COVID-19 Waivers for Food and Nutrition Service Programs
  - 14.862 Indian Community Development Block Grant Program
  - 93.153 Coordinated Services and Access to Research for Women, Infants, Children, and Youth
  - 93.914 HIV Emergency Relief Project Grants
  - 93.917 HIV Care Formula Grants
  - 93.918 Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease
- New non-COVID-19 cluster—Federal Motor Carrier Safety Assistance (FMCSA) cluster (20.218 and 20.237)

For COVID-19-related programs that are not included in the Addendum, auditors should continue to use the guidance in Part 7 of the 2020 Compliance Supplement to identify and document compliance requirements that are applicable, and direct and material, to the program. The practice aids for *PPC's Guide to Audits of Nonprofit Organizations* and *PPC's Guide to Single Audits* include an audit program based on Part 7.

Student Financial Assistance (SFA) Cluster

The compliance requirements for the SFA Cluster are not addressed in detail in the Addendum. However, the Addendum points out that, as a result of the COVID-19 pandemic, there may have been requirements that were waived or changed for certain institutions. Therefore, auditors need to review resources provided by the Department of Education and institution-specific communications in order to determine the appropriate audit steps to test for compliance.

Practical Consideration:

The Department of Education has developed a comprehensive website related to COVID-19 matters that auditors should use as a resource. The website can be accessed at **https://www.ed.gov/coronavirus?src=feature**.

Single Audit Reporting Package Extension

Due to the delayed guidance related to COVID-19 funding that is provided in the Addendum, the OMB has granted a three-month extension to complete and submit the single audit reporting package. The extension is automatically granted to single audits with original due dates from October 31, 2020, through June 30, 2021 (fiscal years ending January 31, 2020, through September 30, 2020) for recipients and subrecipients that received COVID-19 funding during the audit period. No approval is needed to use the extension. However, the reason for the delayed submission should be documented. Entities that take advantage of the automatic three-month extension will still qualify as a low-risk auditee.

Provider Relief Fund and the SEFA

The Addendum clarifies that entities who received and expended (or replaced lost revenue) with the U.S. Department of Health and Human Services (HHS) Provider Relief Fund (PRF) (CFDA/Assistance Listing No. 93.498) will not include those amounts on the schedule of expenditures of federal awards (SEFA) until December 31, 2020, year ends. Therefore, for entities with fiscal year ends prior to December 31, 2020, PRF will not factor into major program determination and is not subject to single audit in that year. (However, these funds would still need to be audited for financial statement purposes and would still be subject to compliance with the terms and conditions of the award.) The PRF expenditures and lost revenue amounts will first be reported in the SEFA and audited under the Uniform Guidance in a fiscal year ending on or after December 31, 2020. The reason for this unusual and inconsistent treatment between entities receiving PRF funding with varying year ends is so that the SEFA reporting will link to calendar year reporting for HHS.

Part 4 of the Addendum provides specific guidance for amounts to report on the SEFA for entities who receive and expend PRF, by their respective fiscal year ends. The following summary outlines PRF SEFA reporting requirements:

- Fiscal years ending before December 31, 2020: Do not report PRF on SEFA.
- Fiscal years ending December 31, 2020: Report based on December 31, 2020 PRF Report.
- Fiscal years ending January 1, 2021, through June 29, 2021: Report based on December 31, 2020 PRF Report.
- Fiscal years ending June 30, 2021, and later: Refer to the 2021 Compliance Supplement for guidance.

For fiscal years ending from December 31, 2020, through June 29, 2021, entities must disclose in the notes to the SEFA that the expenditures (including lost revenue) presented are based on the PRF Report for the calendar year ending December 31, 2020.

Personal Protective Equipment (PPE) and the SEFA

Appendix VII of the Addendum explains that, under OMB Memorandum M-20-20, federal agencies and recipients could donate PPE purchased with federal funds to various entities for use in the COVID-19 response. Because, in most cases, PPE was donated without compliance or reporting requirements, or a related CFDA/Assistance Listing number, the donated PPE should not be reported on the SEFA or factor into major program determination. Instead, the fair market value of the federally funded, donated PPE, at the time of receipt, should be reported in a stand-alone footnote to accompany the SEFA.

Practical Consideration:

The Addendum states that the PPE stand-alone footnote to the SEFA can be marked as "unaudited" since it doesn't affect the single audit and is not required to be audited as a major program.

Other Agency Guidance

Appendix VII also mentions the significant amount of guidance issued by federal agencies outside of the normal regulatory process throughout the pandemic for new and existing COVID-19-related programs. Although auditors may use this guidance to interpret the relevant statutes, regulations, and terms and conditions of federal awards, the guidance doesn't create new compliance requirements. In addition, the Addendum notes that the guidance has been updated and continues to change over time. In many cases, the Addendum contains links to the agency guidance, and also advises the auditor that they may conclude whether or not the auditee is in compliance with a specific compliance requirement based on their consideration of the implementing guidance at the time of the activity or transaction. However, the Addendum emphasizes, that when citing criteria for audit findings, auditors should refer to the statute, regulation, or terms and conditions as the criteria for the audit finding.

Final Regulations on Executive Compensation

Background

For tax years beginning after December 31, 2017, IRC Sec. 4960 imposes an excise tax at the corporate tax rate on applicable tax-exempt organizations (ATEOs) or related organizations (defined later) paying excess compensation to covered employees. Excess compensation is the sum of [IRC Sec. 4960(a)]—

1. any remuneration paid (other than an excess parachute payment) exceeding $1 million for a tax year, and
2. excess parachute payments to a covered employee.

Both proposed and final regulations were released in 2020 that provide comprehensive guidance on IRC Sec. 4960. (The proposed regulations were discussed in the August 2020 edition of this newsletter.) The final regulations (T.D. 9938) apply to tax years beginning after December 31, 2021. Organizations can choose to apply them to tax years beginning after December 31, 2017, if they are applied in their entirety and in a consistent manner [Reg. 53.4960-6].

Caution: Compensation plans in place on December 31, 2017, are impacted by IRC Sec. 4960 if remuneration is vested under the plan after December 31, 2017. It does not matter that IRC Sec. 4960 was not required when the compensation plan was executed. That is, there is no transition relief. Even though one commenter suggested that employee remuneration contracts executed on or before November 2, 2017, be grandfathered and, as a result, excluded from IRC Sec. 4960, the final regulations do not provide for grandfathering.

ATEO Definition Modified

An applicable tax-exempt organization (ATEO) is one that for the tax year [IRC Sec. 4960(c)(1), Reg. 53.4960-1(b)(1)]—

1. is exempt from tax under IRC Sec. 501(a),
2. is a farmers' cooperative organization described in IRC Sec. 521(b)(1),
3. has income excluded from tax under IRC Sec. 115(1) (e.g., income of public utility companies, states, or municipalities), or
4. is a political organization described in IRC Sec. 527(e)(1).

Foreign organizations and their related organizations. The final regulations clarify that a foreign organization that is both (1) described in IRC Sec. 4948(b), and (2) is either exempt from tax under IRC Sec. 501(a) or is a taxable private foundation is not an ATEO. Additionally, a foreign organization's status is determined at the end of its tax year [Reg. 53.4960-1(b)(2)].

However, while the Section 4960 excise taxes do not apply to these foreign organizations, their payments to a related organization's covered employee may subject other organizations to the excise tax. Remuneration paid to an ATEO's covered employee by a foreign related organization must be taken into account in determining the ATEO's liability for the Section 4960 excise tax, and the ATEO's five highest-compensated employees. For example, if an ATEO and its related foreign organization under IRC Sec. 4948(b) each paid $600,000 remuneration to a covered employee during the applicable year, then the foreign related organization would not be liable for the tax that would otherwise be allocable to it, and the ATEO would be liable for tax on $100,000 (50% of the $200,000 excess remuneration paid to the employee) [Reg. 53.4960-4(a)(4)].

Federal instrumentalities. The Treasury Department and the IRS consider all federal instrumentalities described in IRC Sec. 501(c)(1) to be included in the statutory ATEO definition as an organization exempt from tax under IRC Sec. 501(a) and therefore subject to Section 4960. See the August 2020 edition of this newsletter that discusses the clarification provided in the proposed regulations about the treatment of government entities. The final regulations did not provide guidance on organizations described in IRC Sec. 501(c)(1)(A)(i) (e.g., federal credit unions, FDIC, CCC, or PBGC); they reserved guidance for these organization for future regulations. Until then, these entities can treat themselves as not subject to tax under IRC Sec. 4960 as an ATEO or related organization. But, if it is a related organization to an ATEO [defined in Reg. 53.4960-1(i)], the remuneration it pays to covered employees is taken into account by the ATEO.

Covered Employee and the Five Highest

Covered employees include any employee (including any former employee) of an ATEO if the employee [IRC Sec. 4960(c)(2)]—

1. is one of the organization's five highest paid employees for the tax year, or
2. was the organization's (or a predecessor's) covered employee for any preceding tax year beginning after December 31, 2016.

An employee is not required to be an officer to be considered a covered employee. Additionally, an employee can be a covered employee even though he or she is not paid excess remuneration, an excess parachute payment, or is a highly compensated employee under IRC Sec. 414(q).

Note: Once an employee is determined to be a covered employee, that employee remains a covered employee for future tax years. Therefore, the ATEO should maintain detailed employee records on these employees.

Five highest-compensated employees. Determining if an employee is one of the five highest-compensated employees is based on his or her remuneration paid during the calendar year ending with or within the ATEO's, or related organization's, tax year. The five highest-compensated employees are determined separately for each ATEO and not for the entire group of related organizations. Therefore, a related group of ATEOs can have more than five highest-compensated employees for a tax year. An employee may be a covered employee of more than one ATEO in a related group of ATEOs in a tax year.

The final regulations modify the nonexempt funds exception (discussed in the August 2020 edition of this newsletter) by expanding the measurement period for the exception from one to two years (i.e., the current year and the preceding year) for determining whether an employee provided services to the ATEO and all related organizations for less than 50% of the total hours worked [Reg. 53.4960-1(d)(2)(iii)]. An ATEO can make this determination based on the total days the individual worked as an employee rather than on the number of hours worked. But, any day that the individual worked at least one hour as an employee of the ATEO or a related ATEO is treated as a day. Additionally, the final regulations modify the attribution rules by disregarding the downward attribution in applying IRC Sec. 318.

Remuneration Clarified

Remuneration was also covered by the proposed regulations. (See the August 2020 edition of this newsletter.) The final regulations clarify that remuneration does not include foregone interest amounts on below-market loans not exceeding $10,000 that are excluded from gross income under the IRC Sec. 7872(c)(3) *de minimis* exception [Reg. 53.4960-2(a)(1)]. Slight clarifications to the guidance for allocating remuneration for medical and non-medical services are made in Reg. 53.4960-2(a)(2)(ii). Additionally, payment timing is clarified allowing employers to include vested amounts paid within 90 days of the tax year end to be included in the current tax year's remuneration without discounting (e.g., a bonus that vests on December 31, 2022, and is schedule to be paid on February 15, 2023, may be treated as 2022 renumeration) [Reg. 53.4960-2(e)(2)].

Note: The final regulations do not address the coordination of IRC Sec. 4960 and IRC Sec. 162(m) but rather reserve a section of the final regulations (Reg. 53.4960-5) as a placeholder for further guidance. Until that guidance is issued, taxpayers may use any reasonable, good faith approach in dealing with timing differences between when the right to the remuneration vests and when it is paid [and potentially disallowed by IRC Sec. 162(m)].

Form 990-T Revised

The 2020 Form 990-T [Exempt Organization Business Income Tax Return (and Proxy Tax Under Section 6033(e))] has been redesigned to accommodate the electronic filing mandate and the changes implemented by the 2017 Tax Cuts and Jobs Act (TCJA) and subsequently modified by the Coronavirus Aid, Relief, and Economic Security (CARES) Act. Perhaps most notable among these changes is the separate treatment of each trade or business ("siloing") under IRC Sec. 512(a)(6) and its effect on net operating losses (NOLs). These changes have been the subject of several articles in recent editions of this newsletter (including June, July, and August 2020; and January and February 2021).

Reporting Separate Trades or Businesses

Organizations with more than one unrelated trade or business must compute unrelated business taxable income (UBTI), including when determining any NOL deduction, separately for each trade or business. For 2020 returns, a new Form Schedule A (Form 990-T) (Unrelated Business Taxable Income From an Unrelated Trade or Business) is used to report the activity of each separate unrelated trade or business. Each separate unrelated trade or business (UTB) is reported on line 18, Part II of each Schedule A (Form 990-T).

NOL Deductions

NOLs occurring in tax years beginning after 2017. Post-2017 NOLs may only be applied (in a carryback or carryforward) against income from that same unrelated trade or business. The NOL deduction is reported on line 17, Part II of Schedule A (Form 990-T). As discussed in the January and February 2021 editions of this newsletter, the transition from the use of six-digit NAICS codes to two-digit NAICS codes may allow an exempt organization to combine trades or businesses that they previously separated. However, if a separate unrelated business changes its identification (NAICS code), none of the NOLs from the previously identified separate

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unrelated trade or business will be carried over to the newly identified separate unrelated trade or business. The loss is suspended and can be used by a new unrelated trade or business using the same two-digit NAICS code [Reg. 512(a)-6(h)].

Siloed NOLs from 2018, 2019, or 2020 can be carried back to years before 2018 when IRC Sec. 512(a) (6) did not apply (and can therefore offset any UBI). NOL carrybacks were discussed in the August 2020 edition of this newsletter.

Note: Organizations with NOLs in 2018, 2019, or 2020 could elect to waive the carryback period.

Practical Consideration:

Careful attention must be given to the grouping by two-digit code for Form 990-T reporting.

The UBTI from line 18, Part II of Schedule A (Form 990-T) for any unrelated trade or business cannot be less than zero when computing total (aggregated) UBTI reported on line 1, Part 1 of Form 990-T (i.e., a siloed NOL cannot be used to offset another unrelated trade or business).

Tax Briefs

FORM 1024-A MUST BE FILED ELECTRONICALLY. As noted in the January 2021 edition of this newsletter, the IRS has revised the Form 1024-A [Application for Recognition of Exemption Under Section 501(c)(4)] to provide for electronic filing. The IRS began accepting electronic submissions January 5, 2021. During a 90-day grace period paper forms will be accepted. However, beginning April 5, 2021, all Forms 1024-A are required to be e-filed. Final instructions for the form are available at **www.irs.gov/pub/irs-pdf/i1024a.pdf**.

IRS COMPLIANCE INITIATIVES FOR FISCAL YEAR 2021. The tax-exempt sector (TE/GE) of the IRS has released the IRS Fiscal Year 2021 Program Letter. Updated information and initiatives will be added online throughout the year. The most recent information indicates TE/GE will be focusing on worker classification, excise tax on excess compensation, certain employee plan issues, and arbitrage violations of tax-exempt bonds. The compliance initiatives are located at **www.irs.gov/government-entities/tax-exempt-government-entities-compliance-program-and-priorities#cs**.

SELF-DECLARED EXEMPT ORGANIZATIONS AND TAX-EXEMPT STATUS. The IRS has determined that certain tax-exempt organizations and self-declared exempt organizations (e.g., churches, small public charities, pre-October 10, 1969 organizations) that do not file for tax exemption within 27 months of their creation cannot request Section 9100 relief for their late-filed applications. Because Section 9100 applies only to late-filing organizations that are required to file for exemption, self-declared organizations do not qualify for this relief. As a result, organizations that are not required to file for exemption but submit an application and miss the 27-month application window cannot have their requests for tax exemption apply retroactively to their organization date. Additionally, these organizations do not have a right to appeal under IRC Sec. 7428 if their exemption is denied.